

From: Morby, Greg C [GMorby@chevrontexaco.com]
Sent: Monday, November 10, 2003 3:00 PM
To: MRM Comments
Cc: Daboval, Wendy F
Subject: Federal Oil Valuation Proposed Rule Comment

<<MMS Crude Oil Comments 11-10-2003 for email submission.asc>>

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11/13/2003

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VIA E-MAIL (MRM.comments@mms.gov)

Attn: "Federal Oil Valuation Proposed Rule Comment"

and

FACSIMILE (303-231-3781)

ORIGINAL TO FOLLOW BY REGULAR MAIL

Ms. Sharron L. Gebhardt
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MINERALS MANAGEMENT SERVICE FEDERAL OIL VALUATION PROPOSAL,
30 CRF Parts 206 and 210, 68 FR 50087 (Aug. 20, 2003)

Dear Ms. Gebhardt:

ChevronTexaco Exploration & Production Company, a division of Chevron U.S.A. Inc ("ChevronTexaco") appreciates the opportunity to comment on the subject notice reopening the public comment period on MMS's Oil Valuation Proposed Rule (68 FR 50087). As one of the largest payors of royalties on oil produced from federal leases, ChevronTexaco is significantly affected by the Proposed Rule.

ChevronTexaco endorses and incorporates by reference the comments filed in response to this proposal by the Royalty Strategy Task Force dated November 10, 2003. In particular, ChevronTexaco calls the attention of the MMS to Section 9 of those comments, found at page 5, "Lessee opt-in to indexing for certain arm's length transactions". We augment that discussion with the following further comments.

ChevronTexaco encourages MMS to provide an index option to value arm's length sales downstream of the lease. Allocation of sales back to multiple leases based on weighted average prices and transportation costs ("tracing") is impractical and in many cases impossible to perform on a contemporaneous basis, irrespective of whether the lessee sells production to an affiliate, or participates in multiple downstream direct sales to third parties. To the degree that compliance with the proposal may be an impossibility, the proposal may be unenforceable.

Lessees who sell production away from the lease should have the option of valuing production based on gross proceeds or the index methodology. MMS failed to address this issue in its March 15, 2000 Final Rule (65 FR 14022) and has the opportunity to remedy its discriminatory effect at this juncture.

Under the current rule, "Gross proceeds" means the total consideration accruing for the disposition of oil produced.

30 CFR 206.101. The value of oil sold by a lessee or its affiliate pursuant to an arm's length contract will be the gross proceeds accruing to the seller. 30 CFR 206.102(a). Therefore, MMS makes no distinction between a proceeds to a lessee and proceeds to an affiliate for purposes of determining gross proceeds to the seller.

Where there are multiple arm's length contracts to sell oil from a lease, they must be weight-averaged. 30 CFR 206.102(b). In response to comments that tracing gross proceeds would be overly burdensome, MMS provided in the current rule, an option to use index in lieu of tracing gross proceeds through one or more exchanges. 65 FR 14036, 14041, 14047; 30 CFR 206.102(d)(1). MMS also provided an option to use index in lieu of tracing gross proceeds where the lessee transfers to an affiliate who resells the oil at arm's length. 65 FR 14063.

In each case where the option to use index or gross proceeds is available, MMS employs a single reason to justify the option, i.e., "the potential administrative burden of tracing." 65 FR 14047. However, the current and proposed rule fail to address the indisputable burden of tracing for lessees who market production via multiple arms length contracts at multiple locations, i.e., in exactly the same manner as affiliates. The burden of tracing is exactly the same irrespective of whether the arm's length multiple sales are entered into by a lessee or by an affiliate. If tracing is a burden for an affiliate, or for a lessee who enters into an exchange agreement, it is no less a burden for a lessee who markets its own production. If the administrative burden of tracing justifies an option for affiliates and for exchange agreements, then it justifies the option for lessees without affiliates.

Gaming can be prevented by applying the same limitations on the option that exist for affiliates and for lessees who use exchanges, i.e., 2-year election applicable to all of the lessee's production from a unit, communitization agreement or lease.

There is a legitimate need to use an index in lieu of tracing gross proceeds. The underlying premise of the current rule is that indices, adjusted for location and quality, represent the true market value of production at the lease. As MMS states, the index option subject to the 2 year limitation "preserves the integrity of the rule's underlying principle of applying arm's length gross proceeds where appropriate, but still allowing use of index/benchmark values that fairly represent market value where `tracing' would be too burdensome." 65 FR 14047.

ChevronTexaco's experience supports a conclusion that prices obtainable in arm's-length sales at downstream points do not vary widely enough from published spot prices to warrant tracing. We believe that an examination by MMS of the valuation data collected from multiple payors would confirm this and urge MMS to undertake such an analysis. Allowing an index option for lessees who market their own production via multiple dispositions would be no more a retreat from the gross proceeds rule than it is for lessees who sell their production to affiliates, or following one or more exchange agreements.

Respectfully submitted,

{original signed by GC Morby}

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